United States Court of Appeals

for the Second Circuit

EXHIBITS

77-7125/26

In The

United States Court of Appeals

For The Second Circuit

77-7125/7126

DOROTHY L. COLE, LOIS H. ZISOOK, HARRY W. VOEGE and ANNA MAY TUNMORE, as Trustees, SAMUEL GREENFIELD FUND, INC., and HAROLD STILLER and MILDRED STILLER, as joint tenants,

Plaintiffs,

HARRY W. VOEGE and ANNA MAY TUNMORE, as Trustees,

Plaintiffs-Appellants,

vs.

SCHENLEY INDUSTRIES, INC., GLEN ALDEN CORPORATION, RAPID-AMERICAN CORPORATION, ISIDORE A. BECKER, BERNARD GOLDBERG, PAUL A. JOHNSTON, DAVID A. CHERNOW, WALTER O. HEINZE, HOWARD FELDMAN, MILO B. HOPKINS, RUSSELL G. SMITH, ALBERT N. GREENFIELD, MESHULAM RIKLIS, GLEN ALDEN SUBSIDIARY, INC., P.J. CLIFFORD, W.P. JOHNSON, S. KITTAY, M.L. MENDELL, L.C. LANE, G.H. PERKINS, and B. DENMARK,

Defendants-Appellees.

On Appeal from the United States District Court for the Southern District of New York.

EXHIBITS (VOL. II
Pages A1475-A1504)

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PLAINTIFF'S EXHIBIT 49 - AFFIDAVIT OF STANLEY S. SHUMAN
SWORN TO JUNE 7, 1971 (pp. 1-28)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

HARRY WALTER VOEGE and ANNA MAY TUNMORE, as Trustees under the Last Will and Testament of Harry W. Voege, Plaintiffs, -against- R. G. SMITH, M. B. HOPKINS, B. GOLDBERG, A. N. GREENFIELD, I. A. BECKER, B. DENMARK, W. O. HEINZE, P. A. JOHNSTON, D. A. CHERNOW, H. S. FELDMAN, P. J. CLIFFORD, W. P. JOHNSON, S. KITTAY, M. L. MENDELL, L. C. LANE, G. H. PERKINS, M. L. RIKLIS, SCHENLEY INDUSTRIES, INC., and GLEN ALDEN CORPORATION, Defendants.	71 CIV. 1042 AFFIDAVIT

STATE OF NEW YORK)
) SS.:
COUNTY OF NEW YORK)

STANLEY S. SHUMAN, being duly sworn, deposes and says:

1. I am an Executive Vice President, Director and member of the Executive Committee of Allen & Company Incorporated, investment bankers, located at 30 Broad Street, New York City. I am primarily concerned with the area of corporate finance, including particularly participating in investment decisions for private investments by Allen & Company Incorporated, and the rendering of advice to a wide variety of corporations with respect to mergers, acquisitions and financings. These duties involve

me on a daily basis in the valuation of companies and their securities. I received an LL.B degree from Harvard Law School in 1959, and an MBA degree from the Harvard Graduate School of Business Administration in 1961. I have been with Allen & Company Incorporated since its formation in October, 1964 and prior thereto, since October 1961, with an affiliated partnership of Allen & Company Incorporated.

2. I make this affidavit on behalf of Schenley Industries, Inc. ("Schenley") in opposition to the motion by plaintiffs in this action for a temporary injunction, in which plaintiffs contend that a proposed reorganization involving Schenley and Glen Alden Corporation ("Glen Alden"), Schenley's majority shareholder, will be grossly unfair to Schenley's minority shareholders. I would like at the outset to state my conclusion that there is no foundation to this claim and that plaintiffs' contentions are, in my opinion, contradicted by all of the relevant market facts and financial criteria.

Prior Relationships

3. It should be noted that Allen & Company Incorporated and an affiliated partnership have from time to time performed investment banking services for Glen Alden and its related companies. We acted as a co-dealer-manager for Glen Alden in its exchange offer made to holders of Schenley common shares in August 1968, and also rendered advice to Glen Alden in connection with that offer, for which we received aggregate compensation in the amount of approximately $328,500. In addition, we advised Glen Alden with respect to its merger with Philip Carey Corporation in

1967, and with respect to its purchase of shares of stock of Stanley Warner Corporation in 1967; we acted as a managing underwriter in connection with the sale of industrial revenue bonds for subsidiaries of Glen Alden in 1967; we rendered financial advice to McCrory Corporation under a four-year retainer agreement which ended in February 1969, and to Lerner Stores Corporation under a three-year agreement which ended in December 1969; we co-managed the underwriting of McCrory's sale of a portion of its Lerner shares in 1966; and we acted as co-dealer manager for Rapid-American Corporation's exchange offer to Glen Alden shareholders in February 1969. Our aggregate compensation for these services (excluding Glen Alden's exchange offer for Schenley common stock) was approximately $1,200,000, which figure includes our net profits from the sale of certain of the underwritten securities. We expect that we may render other investment banking services to Glen Alden and its affiliates in the future.

4. In reaching my conclusion, I studied relevant data concerning Schenley, including published financial data and other material relevant to Schenley's operations and information relating to the liquor industry, with special reference to Schenley's relative position in that industry. In this connection, I considered particularly data as to trends in consumption of various types of liquors and as to relative brand strengths within the industry, including material concerning trends in sales of leading brands throughout the last 20 years. In addition, I met with appropriate members of Schenley's management to discuss

various matters considered pertinent, including Schenley's sales, inventory and accounting practices. Much of the material on Schenley's operations and practices and on the liquor industry was furnished to me at my request by Schenley, and I did not make any independent factual investigation of the accuracy of this material. I was also furnished by Glen Alden, at my request, with information which I considered in determining the value of the Glen Alden debentures to be offered to Schenley's minority shareholders.

The Proposed Reorganization

5. Under the terms of the proposed reorganization, public stockholders of Schenley will receive the following consideration: holders of Schenley common stock will receive $5 in cash plus $30 principal amount of the 14-year Glen Alden 7 1/2% subordinated sinking fund debentures (the "7 1/2% Debentures") for each share owned, while holders of Schenley $1.40 preferred stock will receive $4.50 in cash plus $27 principal amount of the 7 1/2% Debentures for each share owned. Subsequent to our retention by Schenley in early March of 1971 (which was after the proposed reorganization in principle had been announced), I had several meetings with Schenley's Chairman of the Board, during which I participated in formulating the detailed terms of the reorganization. Subsequently, I advised the Board that, in my opinion, the terms were fair and equitable to all Schenley

shareholders.*

Valuation of Consideration to be Received

6. It is my opinion that the fair market value of the 7 1/2% Debentures, as of February 25, 1971, the date on which the proposed reorganization was first announced in principle, is approximately 80% of the stated principal amount of the Debentures, so that the consideration to be offered to the holders of Schenley common stock has a value of approximately $29 per share (i.e. $5 in cash and $30 principal amount of 7 1/2% Debentures having a value of approximately $24), and the consideration to be offered to the $1.40 preferred shareholders has a value of approximately $26.10 (i.e., $4.50 in cash and $27 principal amount of 7 1/2% Debentures having a value of approximately $21.60).

7. In arriving at this conclusion, I considered the prevailing price for the presently outstanding Glen Alden 6% Subordinated Sinking Fund Debentures, due 1988, which are listed on the New York Stock Exchange ("the 6% Debentures"). The last reported sale of the 6% Debentures on the Exchange on February 24 was at 60% of principal amount. During the ten prior trading days, the average closing price was 61% of the principal amount, and the bonds traded in a range of 59 3/4%--62% (see Exhibit 1). An investor who purchased the 6% Debentures at those prices would have a current yield (percent of interest per

---

* On February 25, 1971 the Board of Directors of Schenley approved the proposed reorganization in principle subject to certain conditions, including the Board's receipt of a satisfactory opinion of an investment banker. The Board's subsequent approval on March 25, 1971 was made after the detailed terms of the reorganization were formulated. The plan, as finally approved, contains certain modifications suggested by us.

annum to purchase price) of between 9.7% and 10.0%. In addition, the investor who purchased the 6% Debentures would have a yield to average life (i.e. the current yield plus the difference between the purchase price of the debenture and the principal amount payable at maturity amortized as interest over the average remaining life of the bond giving effect to sinking fund payments)of between 11.1% and 11.5%(see Exhibit 2). If the 7 1/2% Debentures were valued by the market on the same yield basis as the 6% Debentures, (without considering the other comparative factors discussed below), the 7 1/2% Debentures would trade between 75% and 79% of principal amount.

8. However, the 7 1/2% Debentures have certain features that make them clearly more valuable than the 6% Debentures. Following the issuance of the 7 1/2% Debentures in the proposed merger, sinking fund payments on the 7 1/2% Debentures begin in the first year, and will result in approximately 45% of the principal amount of the issue being redeemed before any sinking fund payments on the 6% Debentures will be required to be made. (See Exhibit 3) Moreover, as a result of the operation of the sinking fund, the entire issue of the 7 1/2% Debentures will have an average life of 9.7 years and at their maturity only $74,069,124 (22%) of the 6% Debentures will have become payable (see Exhibit 3). Finally, holders of the 7 1/2% Debentures may use them at their face value (i.e. stated principal amount) to exercise any publicly traded warrants that Glen Alden may hereafter issue. Although Glen Alden

has indicated that it has no present intention to issue any such warrants, it should be noted that the other major public companies in the Rapid-American group (including Rapid-American Corporation, McCrory Corporation and Lerner Stores Corporation) have chosen to issue warrants which are presently outstanding and publicly traded. Debentures which can be used at face value to exercise warrants of the issuer generally sell at higher prices than they otherwise would without this feature, since the holder of a debenture selling at below face value can thereby, in effect, exercise the warrants at a discount (i.e. get credit against the exercise price for the face value of the debenture even though it could only be sold at a discount in the market). Other persons exercising warrants would have to pay an amount in cash equal to the exercise price of the warrants.

9. In determining the value of the 7 1/2% Debentures, I also examined prices of comparable debentures of other issuers. As exhibit 4 shows, all of these debentures have later maturity dates than the new debentures, and current yields and yields to maturity which are for the most part lower, and in only one case higher, than the yields which result from the valuation I have ascribed to the 7 1/2% Debentures. The prices at which these debentures are trading, in my opinion, confirm my conclusion as to the value of the 7 1/2% Debentures.

10. For the above reasons, I conclude that the 7 1/2% Debentures should sell on the New York Stock Exchange at approximately 80% of the stated principal amount.

Valuation of Consideration to be Received by Preferred Shareholders

11. In considering the amount to be received by the holders of the $1.40 preferred stock, I have treated the holder of one preferred share as if he held .9 shares of common stock, i.e., the fraction of a share of common stock into which one share of preferred stock is convertible. Thus, I have valued the preferred stock at their conversion value, and have assumed that the value of the preferred stock will be determined by the value of the common stock. Although preferred stocks sometimes sell at a premium over their conversion value, the Schenley convertible preferred stock has sold virtually at parity (i.e. 90% of the price of the Schenley common stock) since its issuance (see Exhibit 5). Moreover, since the convertible preferred stock is redeemable by Schenley at its option at $24 per share, a holder of a share of convertible preferred stock would be forced to convert the stock into 9/10 of a share of common stock, or face economic loss if Schenley elected to call the convertible preferred stock at any time the price of the common stock exceeded $26.67. On February 24, 1971, the closing price on the New York Stock Exchange of the preferred stock was $26 7/8 per share and the price of the common stock was $29 1/4. Under these circumstances, there would be no reason for the Schenley convertible preferred stock to trade at a premium over the value of 9/10 of a share of common stock. Accordingly, the following discussion, and the valuation criteria set forth herein, apply to the preferred stock as well as to the common stock,

and the preferred stock will not hereafter be separately discussed and evaluated.

Fairness of the Consideration

12. In my opinion, a value of approximately $29 per share of Schenley Common Stock is fair and equitable to Schenley's shareholders. In arriving at my conclusion, I took into consideration the many traditional indicia of value, including present and historical market prices, and factors relating to earnings, including price-earnings ratios, as well as information relative to the company's future prospects, and data concerning the company's inventory and accounting practices, its product mix and brand strengths and weaknesses, as compared to other companies in the liquor industry. I also considered the factor of book value, including the ratio of book value to market price at which Schenley stock has historically sold, and the factor of the annual income to be received by each Schenley shareholder in the proposed reorganization as compared with the amount presently received as dividends.

Market Price

13. Of prime importance, of course, is the factor of present and historical market price, a consideration which is generally of over-riding significance in valuing securities, such as Schenley stock, which are traded on the New York Stock Exchange. Tested by this standard, the proposed reorganization is demonstrably fair and reasonable.

14. The value of approximately $29 per share to be received is in excess of the average closing price for Schenley common shares from the beginning of 1971 to the announcement of the reorganization on February 24 of $28 3/8, during which time closing prices have ranged from $25 to $31 3/8 (See Exhibit 6). Schenley stock did not trade over $28 during all of 1970, or in the latter months of 1969, and traded as low as $19 1/4 in 1970 and $20 3/4 in 1969. Thus, for approximately the last one and one-half years, Schenley stock has generally sold at a price well below that now being offered. Moreover, during the period from 1960 through 1966, Schenley stock generally sold substantially below $29 per share (as adjusted to take into account the 3-for-2 split in March of 1969). While the stock reached a high of approximately $29 3/8 in 1966, this was the record high for Schenley's shares to that date. Its lowest price during that year was approximately $16 5/8, and the prevailing prices generally throughout the 1960-1966 period were from $15 to $25 per share (see Exhibit 6A).

15. It is my opinion that the price of Schenley's stock during portions of 1967 and all of 1968 was distorted by repeated reports of takeover and merger proposals, starting with a proposed merger agreement with Lorillard Corporation in March 1967, continuing with competing proposals by Glen Alden and Lorillard, and culminating in the successful exchange offer by Glen Alden in late 1968. During this abnormal period, the shares rose to a high of $46 1/4 in July 1967, and to an all-time high of $57 shortly after the Glen Alden exchange offer was made in August 1968. The contest for control of Schenley during this period resulted

in a bidding up of the market price to what was, in light of Schenley's historic performance, an inflated level. I, therefore, gave little weight to the market price during this unusual period, in light of the consistent pattern established during all normal periods, both before and after the competition for control.

16. Within nine months after the completion of the exchange offer on August 31, 1968, the price of Schenley shares declined to its historical "pre-contest" level, where it has remained for the past one and one half years. Since the issuance of Schenley's $1.40 convertible preferred stock as the result of a merger involving Schenley and The Buckingham Corporation ("Buckingham") in December 1969, there have been the equivalent of 3,361,000 shares of Schenley common stock listed on the New York Stock Exchange, with a combined average daily trading volume of 5,500 shares (see Exhibit 7), and there are presently approximately 17,500 holders of record. The prices over this extended period, therefore, reflect the arm's-length judgment of many willing sellers and buyers as to the value of Schenley shares. Since value of a security, in the last analysis, reflects the judgment of the market place, the market price of Schenley shares during this period is the primary determinant of the value of Schenley shares in this situation.

The Factor of Earnings

17. The consideration to be received by Schenley shareholders is, in my opinion, demonstrably fair and equitable in the light of Schenley's past and prospective earnings.

In 1970, Schenley had earnings per share (after dilution for full conversion of the $1.40 preferred stock) of $2.64. However, a far more significant figure is Schenley's earnings when appropriately adjusted to reflect the sale of its subsidiary, Buckingham, as recently consummated pursuant to the requirements of a court decree in an anti-trust action. Buckingham is the exclusive United States importer, under a long-term license, of Cutty Sark Scotch Whisky, the country's first or second leading Scotch whisky in sales in 1970.

18. Buckingham's net income (exclusive of interest income) in 1970, was approximately $8,600,000, or approximately 32% of Schenley's total net income.

19. In the computation of earnings adjusted for the sale of Buckingham, as is shown in Exhibit 8, the net proceeds from the sale of Buckingham are used to reduce Schenley's short term debt at Schenley's average interest cost for last year of 8.3%, resulting in earnings per share of $2.18. With interest rates down substantially this year, the actual interest savings should be almost two percentage points less so that the adjusted earnings per share would be correspondingly reduced.

20. I believe it will be difficult for Schenley to invest the proceeds of the sale of Buckingham in going concerns at higher returns. The terms and conditions of the consent decree prohibit Schenley from acquiring for ten years any rights to import and sell, or produce and sell, any additional brands of Scotch whisky whether bottling is done here or abroad (a copy of the decree is attached as

Exhibit 9 hereto). In addition, I have been advised by counsel to Schenley that Justice Department and FTC Guidelines potentially limit the size of possible acquisitions by Schenley in other areas. Finally, Schenley's management has had no significant operating experience in other industries. It would accordingly appear that Schenley's growth will have to come from its present business augmented by the introduction of new brands and products, the success of which is by no means assured.

21. Utilizing the $2.64 and $2.18 figures, the proposed reorganization will provide Schenley's shareholders with a consideration equivalent to a price-earnings ratio of approximately 11 if Buckingham's earnings are included or of approximately 13 when, as is appropriate, the sale of Buckingham is taken into account.

22. In my opinion, these price-earnings ratios for Schenley are fair and equitable. Such ratios are in excess of the price earnings ratios at which Schenley's stock has historically sold (see Exhibit 10). Thus, for example, during 1970 Schenley's price earnings ratio varied from 7 to 11, and the same pattern was demonstrated in the latter part of 1969 after the stock had resumed its normal pattern following the contest for control of Schenley between Glen Alden and Lorillard. Similarly, during the two-year period prior to the contest for control, Schenley's price-earnings ratio fluctuated in 1966 from 6 to 11, and in 1965 between 7 and 12. Thus, Schenley's shareholders are receiving a price that is in excess of that which would

be warranted under Schenley's historical price-earnings pattern.

23. Exhibit 10 also shows the price-earnings ratios of other alcoholic beverage companies. It should be noted that several of these companies have significant operations in areas outside the liquor industry and are therefore not directly comparable to Schenley. For example, Distillers Corp.-Seagrams has substantial oil and gas investments, and National Distillers also manufactures chemicals, textiles, plastics and brass and copper products. Hublein has substantial food product operations, and its distilled spirits business is concentrated predominantly in vodka, where it is by far the major factor in the U. S. market. Standard Brands is among the largest packaged food companies; distilled products accounted for only 15% of its sales in 1969. Nevertheless, a price earnings ratio of 13 is within the range of ratios shown on Exhibit 10, although it is in the low end of the range.

24. There are a number of reasons why Schenley merits, in my opinion, a price-earnings ratio in the low end of the range of the ratios obtaining in the liquor industry.

25. First, and most important, Schenley's historical record of earnings growth as compared to that of the liquor industry generally is distinctly unimpressive. Generally speaking, a price-earnings ratio reflects the market's estimate of the potential for future growth of a company, and companies with limited growth and growth potential tend to have lower price earnings ratios. As is indicated in

Exhibit 11, Schenley's earnings per share from 1966 through 1970 increased at a compound rate of only 4% even when earnings of Buckingham are included. This ratio of growth is distinctly poorer than the better performing companies in the industry. Moreover, if earnings of Buckingham are excluded, as they must be in any realistic appraisal of Schenley today, Schenley's rate of earnings growth, as indicated in Exhibit 11, has been infinitesimal during this period. Even this does not give a complete picture of Schenley's poor earnings growth history, however, since Schenley's 1969 and 1970 increases in earnings are attributable in substantial part to factors which are not necessarily relevant to Schenley's future growth potential. Approximately 37¢ (15%) of Schenley's 1970 earnings per share are the result of an overhead reduction program which commenced in mid-1968 and continued through mid-1969. The details of this program are described in Exhibit 12. This program had no effect on Schenley's earnings in the fiscal year ended August 31, 1968 and only a partial effect in the calendar year 1969. The full impact of the $7,500,000 savings resulting from the program was first reflected in 1970. Continued growth in earnings of any significant magnitude from this source would appear unlikely.* On the other

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*Schenley's upward trend in earnings in 1970 as compared to fiscal 1968, the last full year under the prior managment is also derived in part from the fact that $6,316,000 of transitional costs relating to marketing and organizational changes were charged to earnings in 1968. It should be noted that this charge, together with the overhead reduction program savings discussed above in the text, substantially equal the approximately $13,700,000 aggregate increase in Schenley's net income before taxes and extraordinary items from fiscal 1968 to 1970.

hand, Schenley's gross margins are likely to erode in the future as the company continues to be burdened by carrying costs on its relatively slow moving inventory of bourbons and blended whiskies, as is discussed in more detail below when the factor of book value is considered.

26. It should also be noted that Schenley's major competitors, Distillers Corp--Seagrams, Hiram Walker and National Distillers, all use a form of the LIFO method of inventory valuation while Schenley uses a form of the FIFO method. If one assumes a gradual inflationary trend, this would result in somewhat of an overstatement of Schenley's earnings relative to its competitors which might well result in lower price earnings ratios.

27. Schenley's poor record of earnings growth, excluding Buckingham, is not confined to the last five years. In a survey of the liquor industry in 1965, Forbes Magazine called Schenley's record at that time "deplorable", and detailed the reasons for its characterization in the chart attached as Exhibit 12a (Forbes Magazine, April 1, 1965, pp. 27-28). As this chart indicates, during the five years between 1959 and 1964, prior to the acquisition of Buckingham, Schenley's sales declined 13.4% and its earnings per share plummeted 45.6%.

28. Schenley's poor growth record in recent years is also reflected in its declining share of the distilled spirits market over the past decade, as is summarized in Exhibit 13. As is indicated in that Exhibit, from 1960 to

1970 Schenley's estimated share of the total distilled spirits market declined over 25% (from 11.5% to 8.5%) and its total case sales increased from 10,025,000 cases to only 11,868,000 cases. Most of this increase occurred in 1969 and 1970, and a substantial part of the increase is represented by Dewars Scotch Whisky, as to which Schenley has only a short term import agency. Moreover, during this ten-year period, Schenley's case sales of its domestic whiskies (bourbons and blends) actually declined from 7,696,000 cases to 6,570,000 cases and its market share of domestic whiskies dropped from 14.7% to 11.3%.

29. A second factor which significantly affects Schenley's price earnings ratio is its product mix. Schenley is heavily concentrated in bourbons and blended whiskies. Approximately 50.3% of Schenley's sales revenues in 1970 (excluding Buckingham) were of bourbons and blends, and approximately 60% of Schenley's total inventory as at December 31, 1970 consisted of bourbons and bulk whiskies to be used in blended whiskies. As Exhibits 14 and 14a indicate, bourbons and blended whiskies have been the slowest growing segment of the distilled spirits industry; blends have dropped from 30.6% of the total distilled spirits consumption to 20.8%, while bourbons have declined from 30.1% to 24.3%. Moreover, as was mentioned above, Schenley's case sales, and percentage of market, of bourbons and blended whiskies have actually declined over the past ten years even though this is its largest area of concentration.

30. As Exhibits 14 and 14a indicate, the most rapidly growing segments of the liquor industry are Scotch

whisky, Canadian whisky, gin and vodka. As is discussed in greater detail below, Schenley does not own any major brands in these areas. Moreover, the recent antitrust decree in regard to the divestiture of Buckingham prohibits Schenley for ten years from acquiring any other brands of Scotch whisky.

31. A third factor affecting Schenley's price earnings ratio is the fact that a substantial portion of Schenley's current earnings, and an even greater portion of its earnings growth in the last few years, are derived from the importation and sale of Dewars Scotch Whisky. Schenley does not own the Dewars brand; it has only an import agency which at the present time has a three-year term. Moreover, this agency is nonassignable, and it is cancellable by the brand owners if control of Schenley should change. (A copy of the agency agreement is annexed as Exhibit 15.) Because of these factors, Schenley's earnings from the marketing of Dewars Scotch Whisky merit, in my opinion, a lower price-earnings ratio than would be the case if the brand were owned by Schenley. An indication of the proper earnings multiple assignable to the Dewars earnings can be derived from Schenley's recently concluded sale of Buckingham. As has been mentioned, Buckingham's principal asset is an import agency under which it has the right to import and sell Cutty Sark. However, unlike the Dewars distributorship, Buckingham's distributorship is for a term ending in the year 2000 and is not cancellable upon a transfer of control of Buckingham. In the sale of Buckingham, Schenley guaranteed that Cutty Sark

Scotch Whisky and Buckingham's other minor products will maintain a level of sales over the next five years which is calculated to produce after-tax earnings for Buckingham of approximately $10,000,000. The purchase price paid for Buckingham was 12 times this guaranteed level of earnings. Accordingly, in my opinion, the price earnings ratio assignable to Schenley's earnings from Dewars should be less than the 12 times guaranteed earnings obtained by Schenley in its recent sale of Buckingham.

32. Another important factor which must be considered in valuing a consumer products company, such as Schenley, is the quality and the degree of public acceptance of its brands. An examination of this factor shows that not only is Schenley unduly concentrated in the segments of the liquor industry of declining popularity, but also that Schenley is deficient in major brands. As estimates of leading brand sales published in the Alcoholic Beverage Executives' Newsletter for March 19, 1971 (Exhibit 16) show, with the exception of Cutty Sark (which Schenley has now sold as a result of a court decree) and Dewars (where Schenley has only a three-year import agency) Schenley's brands do not show the substantial public acceptability which would be the surest foundation for future growth.

33. Thus, it is estimated that 32 brands had case sales of 1,000,000 or more in 1970. Of these brands, Seagram's owned seven, including the top two brands -- Seagram 7 (with 8,000,000 cases sold) and Seagram VO (with 4,400,000 cases sold) -- as well as Calvert Extra (ranked

No. 10 at 2,495,000 cases), Kessler (No. 13 at 2,000,000 cases), Christian Bros. (No. 26 at 1,300,000), Seagram's Gin (No. 27 with 1,225,000 cases), and Four Roses (No. 28 with 1,200,000 cases). Four of these products had greater sales than any of Schenley's brands (other than Cutty Sark, which has been sold).

34. Hiram Walker owned three brands in this top category -- Canadian Club (ranked No. 3 at 3,960,000 cases), Imperial (No. 11 at 2,265,000 cases) and Ten High (No. 16 at 1,900,000 cases) -- all with greater sales than any Schenley brands other than Cutty Sark.

35. National Distillers had five brands in the top 32, including Old Crow (ranked No. 12 at 2,200,000 cases), Gilbey's Gin (No. 15 with 1,975,000 cases), and Windsor Canadian (No. 17 with 1,812,000 cases) -- all with more sales than any brand Schenley currently distributes -- as well as Old Grand Dad (No. 24 at 1,400,000 cases) and Old Taylor (No. 29 at 1,195,000 cases).

36. Heublein owns Smirnoff Vodka, a brand which has increased in popularity from a point where the Alcoholics' Beverage Executives' Newsletter reported no available sales records for it as late as 1954 to a position where it is now fourth in sales with an estimated volume of 3,700,000 cases -- twice the sales of what is now Schenley's leading brand, Dewars. Heublein also owns Heublein Cocktails, a popular line of products in an area of rapid growth, which had estimated sales in 1970 of 1,055,000 cases. According to a prospectus of Heublein dated October 1969,

Smirnoff Vodka and its two other vodka brands accounted for approximately two-thirds of Heublein's total distilled spirits sales.

37. Brown-Forman, a company whose total distilled beverage sales are only slightly more than one-third of Schenley's, nevertheless owns Early Times (ranked No. 14 with 2,000,000 cases) -- again greater than Dewars -- and also owns Old Forester, which had sales of 1,000,000 cases. Brown-Forman also owns Jack Daniels, which is the dominant factor in the Tennessee whiskey market, and is believed to be a major contributor to Brown-Forman's profits in recent years. According to a 1969 prospectus of Brown-Forman these three brands accounted for 70% of its business.

38. By contrast Schenley, despite its large size, owns outright only two brands in the 1,000,000 case or better category--Ancient Age, ranked No. 19 with an estimated 1,575,000 cases, and Schenley Reserve, ranked No. 31 at 1,000,000 cases--and, since the loss of Cutty Sark, has, in addition, only a short term import agency arrangement for Dewars, ranked No. 18 with 1,800,000 cases.

39. Moreover, of the next ten leading brands below the 1,000,000 category, Hiram Walker owned four (Corby's Reserve, Ballantine's, and Hiram Walker Cordials and Gin), National Distillers owned two (Gilbey's Vodka and Old Sunnybrook blend), Seagram's owned one (Wolfschmidt), Heublein owned one (Popov) and Schenley owned none.

40. In sum, the great bulk of Schenley's sales volume consists of a large number of lesser known brands,

without any great public acceptability. Moreover, except for Dewars Scotch Whisky, which has shown considerable growth, Schenley at present lacks any strong brands in the areas of increasing public consumption: Scotch, Canadian, vodka, gin and cordials. Attached as Exhibit 17 are estimates for 1968 and 1969 of case sales of leading liquor brands published in Standard & Poor's Liquor Industry Survey dated October 15, 1970. This exhibit shows substantially the same deficiency of Schenley in major brands as is reflected in the estimates of the Alcoholic Beverage Executives Newsletter attached as Exhibit 16.

41. Schenley's relatively insecure brand position is also highlighted by the sharply declining trend in sales of what were its major brands in the past, as shown by Exhibit 18. Exhibit 18 shows the case sales in 1950 and 1970 of what were Schenley's top five brands twenty years ago; as that exhibit indicates, these brands declined in volume from 6,918,000 cases in 1950 to 1,297,000 cases in 1970-- a decline of more than 80%. The prime example is Schenley Reserve, which, in 1950, was ranked No. 2 with 4,100,000 annual case sales, and now is ranked No. 31 with only 1,000,000 case sales, a decline of over 3,000,000 cases.

42. To summarize, with the exception of Cutty Sark (which has been sold) and Dewars (where Schenley has only a three-year nonassignable import agency, and the earnings resulting therefrom are, accordingly, entitled to a lower price-earnings ratio than if Schenley owned the brand), Schenley has had an unimpressive growth in sales

volume and in earnings, especially after taking account of the substantial contribution to 1970 earnings of its overhead reduction program where future gains are not likely to occur. In view of Schenley's concentration in the relatively declining area of bourbons and blended whiskies, its weak brand position, and its preclusion by an antitrust decree from acquiring any other brands of Scotch whisky, I do not believe it reasonable to conclude that Schenley's past poor growth record will markedly improve in the future. In the proposed merger, Schenley's minority shareholders will be receiving a consideration in excess of 13 times Schenley's earnings as adjusted for the sale of Buckingham. This is well in excess of the price earnings ratio at which Schenley has historically sold and, in my opinion, is fair and equitable.

Book Value

In concluding that the terms of the proposed merger are fair and equitable to Schenley's shareholders, I took into account the fact that the consideration being offered is approximately 82% of Schenley's book value per share as at December 31, 1970 after adjustment for conversion of outstanding preferred stock and approximately 72% after further adjustment for the sale of Buckingham (see Exhibit 18A).

43. Companies in the liquor industry have not shown any consistent relationship between book value and market price. This is demonstrated by Exhibit 19 which shows market price to book value ratios ranging from 38.3% (Glenmore) and 56% (Publicker) to 267.3% (Brown-Forman) and

449.0% (Heublein). Nevertheless, to the extent that this factor has relevance, it clearly confirms the adequacy of the present offer. Thus, the consideration to be received results in a ratio which is well in excess of the market price to book value ratio at which Schenley has historically sold for the last ten years. As Exhibit 20 indicates, the average ratio of market price to book value of Schenley, taking the median price for each of the last ten fiscal years, was approximately 71.0%. More significantly, if the abnormal periods mentioned previously in which there was a contest for control of Schenley are excluded the average ratio of market price to book value was approximately 58.2% --far less than that resulting from the consideration to be received by Schenley stockholders in the proposed reorganization.

44. There are several reasons, in my opinion, why the market has consistently valued Schenley's assets at less than the assets of many of its competitors. As is indicated in Exhibit 21, Schenley has the highest ratios of inventory to sales and of accounts receivable to sales of any company in the liquor industry. Thus, its inventory and accounts receivable have not shown the same revenue producing capacity as the corresponding assets of other companies. Although these ratios have improved somewhat since Glen Alden's acquisition (see Exhibit 22, which shows these ratios as at August 31, 1968), the management of Schenley does not anticipate significant further reductions.

45. In regard to Schenley's inventory values, several factors should be noted:

First, Schenley includes in its book values of inventory carrying costs, such as ad valorem taxes, storage charges and insurance, and the unamortized cost of barrels, rather than expensing carrying costs as incurred and the full cost of barrels as the barrels are filled or dumped, which is apparently the practice of its major competitors; the management of Schenley estimates that approximately $40,000,000 of such capitalized costs were included in its inventory as at December 31, 1970.

Further, as noted, Schenley uses a form of the FIFO method of inventory accounting while its major competitors use a form of the LIFO method. In an inflationary period Schenley's FIFO method would normally produce larger inventory values for the same quantity and quality of inventory than the LIFO method.

In addition, approximately 60% of Schenley's total inventory consists of bourbons and bulk whiskey for use in blended whiskey which, as is noted above, is an area of declining growth in the liquor industry, and an area where Schenley's sales have declined at a more rapid rate than the industry as a whole. According to published information on distilled spirits in bonded warehouses in Kentucky on August 31, 1970 (see Exhibit 23), Schenley, by comparison with its competitors, had by far the largest volume and percentage of total bonded inventory represented by six-year old and older bourbon. This bourbon can, for the most part, only be sold in the present market on the same price basis as bourbons of lesser age despite the fact that its carrying value on Schenley's books necessarily includes evaporation

costs and carrying costs in a greater amount than is included for a bourbon of lesser age.

Dividend Yield and Interest Income

46. Tested by the important factor of annual income, the proposed reorganization is significantly beneficial to Schenley's shareholders. Schenley's common shareholders presently receive dividends at the annual rate of $1.40 per share; such dividends are, of course, subject to revision up or down by decision of the Board of Directors. The proposed offer would give them fixed interest income equivalent to $2.25 per share per annum--an increase of approximately 60%--in addition to the potential return from investing the $5.00 cash portion of the package.

Glen Alden's Prior Tender Offer

47. In reaching my conclusions as to the terms of the proposed merger, I have also taken into account the consideration paid by Glen Alden in March 1968 for the block of Schenley stock owned by Schenley's then chairman, Lewis S. Rosenstiel, and the consideration offered by Glen Alden in August 1968 in a tender offer to the other Schenley common stockholders. In my opinion, the terms of these transactions have little relevance to the fairness of the terms of the proposed merger. Glen Alden's payment to Mr. Rosenstiel included a substantial premium for control, and also reflected the fact that Lorillard was a competing bidder for the Company at that time. Glen Alden's ensuing exchange offer made to all shareholders of Schenley was necessitated by continued competition from Lorillard as well as a con-

tractual obligation in the Rosenstiel purchase agreement to offer to all shareholders of Schenley a package of securities essentially equivalent in value to the cash price paid to Rosenstiel. This offer was, accordingly, merely an extension of Glen Alden's original decision to pay a premium over market value, so as to make them attractive to shareholders.

48. Further, Glen Alden's investment judgment at that time was apparently predicated in large part on the conclusion that it could quickly reduce to cash what was thought to be a substantial amount of relatively unproductive assets, while maintaining the fundamental earning power of the Company. This assumption would seem to have been reasonable after an examination of Schenley's net working capital compared to the rest of the industry, which indicates the Company's relatively heavy inventory and receivable position (see Exhibit 22). Schenley's comparative balance sheets for the period since Glen Alden's acquisition indicate some progress in this direction but not at all in the order of magnitude anticipated by Glen Alden (see Exhibit 24). Hindsight thus far has shown its original thinking to be overly ambitious.

Summary

49. In my opinion, the value of the package offered to the minority shareholders of Schenley is approximately $29 per share of Schenley Common Stock and approximately $26.10 per share of Schenley $1.40 Preferred Stock, based on a comparison of the proposed 7-1/2% Debentures with Glen Alden's currently outstanding 6% Debentures due 1988,

and with bonds of other issuers. This value is fair and equitable to the shareholders. The judgment of investors on the New York Stock Exchange over the years has established a prevailing market price for Schenley's shares which has been remarkably consistent except for abnormal periods when the market price was distorted for reasons unrelated to the Company's performance. The consideration to be received is substantially in excess of that price. The consideration to be received by the stockholders amounts to at least 11 times Schenley's 1970 earnings including Buckingham, and over 13 times Schenley's earnings adjusted for the sale of Buckingham, and will provide stockholders with increased income of more than 60%. In my opinion, these terms are faif and equitable in relation to Schenley's historical price-earnings and book value ratios, particularly when considered in the context of the many factors which indicate Schenley's relatively limited growth prospects.

STANLEY S. SHUMAN

Sworn to before me this

7th day of June, 1971.

Notary Public

CONSTANCE [illegible]
Notary Public, State of New York
No. 31-7815810
Qualified in New York County
Commission Expires March 30, 1972

EXHIBIT 8 - PRO FORMA STATEMENT OF CONSOLIDATED INCOME OF SCHENLEY FOR THE YEAR ENDED DECEMBER 31, 1970

The following summarizes the Schenley statement of consolidated income for the year ended December 31, 1970 and a pro forma statement of such income adjusted to give effect to the sale of Buckingham for $120,000,000 as if such sale had occurred as at January 1, 1970. The pro forma statement of income assumes that (a) all of the $17,000,000 of Northwest notes acquired by Schenley were sold at January 1, 1970 at face amount; (b) $12,500,000 of the proceeds were used to prepay at January 1, 1970 the then outstanding Schenley 3% notes payable to insurance companies, which are required by their terms to be prepaid out of the proceeds of sale; (c) approximately $13,100,000 of the proceeds were used to pay estimated income taxes arising from the sale and $1,000,000 was provided for estimated fees in connection with the transaction, an aggregate of $14,100,000; and (d) the balance of the proceeds of sale were applied as at January 1, 1970 to the reduction of Schenley's short-term debt with commensurate adjustment in interest expense and related estimated income taxes. The assumption made in (d) above is solely for the purpose of indicating the effect of the sale on Schenley's statement of consolidated income and is not intended as a representation that the proceeds of sale will be applied to reduce Schenley's short-term debt.

	(In Thousands)			
	Schenley Year Ended December 31, 1970	Buckingham Year Ended December 31, 1970	Adjustments*	Pro Forma
Revenues ...	$671,821	60,093	-	$611,728
Cost of goods sold ...	525,353	38,390	-	486,963
Selling, advertising and administrative expenses ...	82,223	4,396	-	77,827
Interest charges--net ...	12,912	-	$(8,040)	4,872
Provision for Federal taxes on income ...	24,150	8,597	3,970	19,523
	644,638	51,383	(4,070)	589,185
Income before extraordinary gain	$27,183	$8,710	$4,070	22,543
Extraordinary gain--on sale of The Buckingham Corporation (net of applicable income taxes of $13,100,000)				71,130
Net income ...				$93,673
Primary earnings per share of common stock:				
Income before extraordinary gain	$3.01			$2.42
Extraordinary gain	--			8.99
Net income ...	$3.01			$11.41
Diluted earnings per share of common stock:				
Income before extraordinary gain	$2.64			$ 2.18
Extraordinary gain	--			6.92
Net income	$2.64			$ 9.10

*Reflects reduction in interest of $365,000 on 3% notes payable to insurance companies and $7,675,000 on short-term debt at Schenley's average interest cost on short-term debt during 1970 and related estimated income taxes.

P/E ANALYSIS

ALCOHOLIC BEVERAGE INDUSTRY*

Fiscal Year		1970 EPS	1970 Price H	1970 Price L	1970 P/E H	1970 P/E L	1969 EPS	1969 Price H	1969 Price L	1969 P/E H	1969 P/E L	1968 EPS	1968 Price H	1968 Price L	1968 P/E H	1968 P/E L	1967 EPS	1967 Price H	1967 Price L	1967 P/E H	1967 P/E L	1966 EPS	1966 Price H	1966 Price L	1966 P/E H	1966 P/E L	1965 EPS	1965 Price H	1965 Price L	1965 P/E H	1965 P/E L
12/31**	Schenley	$2.18*** 2.64	28	19-1/4	13 11	9 7	$2.45	44-3/4	20-3/4	18	8	$2.14	57	32-1/4	27	15	$2.69	46-1/4	20-1/2	17	8	$2.59	29-1/8	16-5/8	11	6	$2.28	26-5/8	14-7/8	12	7
9/30	Amer. Dist.	1.28	20-1/2	16-3/4	16	13	1.47	29-1/4	19-1/4	20	13	1.70	30	22-1/2	18	13	1.63	30	19-1/8	18	12	1.71	23	18-1/8	13	11	1.63	23	19-1/2	14	12
6/30	Barton Brands	0.76	10	5-1/4	13	7	0.68	11-3/4	7-5/8	17	11	0.51	11-7/8	6-1/8	23	12	0.62	8-3/8	4-7/8	14	8	0.65	7-5/8	4-1/2	12	7	0.65	6-3/8	4-3/4	10	7
4/30	Brown Forman	1.26	26-1/8	19-3/8	21	15	1.16	22-5/8	16-1/2	20	14	1.11	21-7/8	15-5/8	20	14	1.04	21-1/2	12-3/4	21	12	0.98	22-3/4	12-1/8	23	12	0.90	23-1/2	11-5/8	26	15
7/31	Dist.Corp. Seag.	3.13	51-1/4	37-1/2	16	12	3.04	58-1/2	44-5/8	19	15	2.89	47-3/4	35-7/8	17	12	2.69	37-1/4	30-5/8	14	11	2.57	37	25-1/4	14	10	2.34	38-1/8	30-3/8	17	13
6/30	Glenmore	0.72	15-3/4	11-1/4	22	16	0.63	20-3/4	13-5/8	33	22	0.87	21-1/8	13-7/8	24	16	0.77	18	12-1/8	23	16	0.57	18-3/8	11	32	19	0.89	21-5/8	15-1/8	24	17
6/30	Heublein	1.36	49	28-1/2	36	21	1.21	43-7/8	32	36	26	1.10	43	26-1/2	39	24	1.05	35	18-3/8	33	18	0.94	19	14-1/8	20	15	0.75	14	11-3/8	19	15
12/31	National Dist.	1.13	18-1/4	14	16	12	1.24	22-3/4	16-1/4	18	13	1.19	23-1/4	18	20	16	1.61	24-1/2	18-5/8	15	12	1.55	20-5/8	15	13	10	1.19	17-1/4	13	14	11
12/31	Standard Brds.	2.80	54-1/2	38-1/2	19	14	2.65	51-1/2	42-1/4	19	16	2.48	54-7/8	33	22	13	2.38	41-1/4	32-7/8	17	14	2.19	38-1/8	27-1/8	17	12	1.87	42-5/8	36-3/8	23	19
8/31	Hiram-Walker Good.& Worts	2.82	59-3/4	33	18	12	2.78	49-1/4	36-3/4	18	13	2.57	40-1/4	27-1/4	16	11	2.37	34-5/8	26-1/2	15	11	2.21	34-3/8	23-3/4	16	11	2.01	40-1/2	32	20	16

* Based upon fully diluted earnings

** August 31, 1968 - 5 on reported figures fully diluted

*** Excluding Buckingham

EXHIBIT 10. - PRICE EARNINGS RATIOS (1968, 1969 & 1970) OF LEADING STOCKS - ALCOHOLIC BEVERAGE INDUSTRY

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